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SUBJECT: ECUADOR ECON UPDATE: BOND REPURCHASE; FINANCIAL LIQUIDITY MEASURES; NOBOA'S TAX DEBT

REFTEL A: QUITO 277
B: QUITO 220

¶1. (U) The following is a periodic economic update for Ecuador that reports notable developments that are not reported by individual cables.

Reactions to Government Repurchase Proposal

¶2. (U) On May 1, a group reportedly representing bondholders holding 25% of outstanding Global 2012 bonds (of a total issuance of $510 million) notified the Ecuadorian government that it intended to accelerate principal repayment. Twenty-five percent is the contractual threshold to call for accelerated payment following a default, which would make the outstanding principal and interest payments due immediately.

¶3. (U) Following the announcement of legal action, Finance Minister Viteri held a conference call with bondholders on May 5. She stated that Ecuador has financing available to repurchase the outstanding 2012 and 2030 bonds under the modified Dutch auction proposal that it announced on April 20 (reftel a). She also stated that Ecuador might pay a higher final clearing price than the 30% floor price set by the GOE. The deadline for bondholders to accept the GOE's modified Dutch action proposal is May 15, and final results of the auction will be announced on May 26.

Government Measures to Improve Liquidity

¶4. (U) Since November 2008, deposits in the banking system have declined markedly. Deposits are down 5.6% or USD 705 million as of early May (in contrast to previous years when deposits were growing at 20% per year). This is largely the result of decreased dollar income because of low oil prices, falling remittances, and weakening non-petroleum exports (reftel b). The Ecuadorian government announced several measures to improve financial sector liquidity. One measure, already announced in March 2009, is for the Ecuadorian Social Security Institute (IESS) to buy up to $500 million in mortgages issued by private banks. Additional measures to improve liquidity include: i) public institutions would refrain from withdrawing their deposits from private banks; ii) a possible increase of IESS deposits in private banks, which now account for $730 million or 5 percent of bank deposits; and iii) the GOE could provide "indirect" support to help financial institutions obtain external financing through regional international financial institutions. In addition, public institutions would accept lower interest rates on their deposits in private banks (up to 4 percent), to help private banks maintain their profit margins.

¶5. (SBU) However, the GOE is considering other actions that could reduce liquidity for some institutions. For example, although public institutions are not to withdraw their deposits from private

banks, Coordinating Minister for Economic Policy Diego Borja threatened to withdraw public sector resources if banks are reluctant to grant credit. In addition, President Correa has presented a bill to reform the Reserve Fund Law, which would drain companies' liquidity by forcing them to pay on a monthly basis employee benefits that were previously paid out every three years.

Banana Magnate Owes Millions in Back Taxes

¶6. (U) The Ecuadorian tax service (SRI) announced recently that Exportadora Bananera Noboa, a banana export company owned by magnate and four-time presidential candidate Alvaro Noboa, owed around $59 million in outstanding taxes from 2005. The head of the SRI also said that the SRI will carry out additional audits on the company for 2006, 2007 and 2008.

HODGES